

ISSUE DATE: August 14, 2000

DOCKET NO. G-999/AA-98-332

ORDER EXTENDING VARIANCES

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

**Gregory Scott
Edward A. Garvey
Joel Jacobs
Marshall Johnson
LeRoy Koppendrayer**

**Chair
Commissioner
Commissioner
Commissioner
Commissioner**

**In the Matter of the Request to Vary
Supplier Refund Rules Regarding a Kansas
Ad Valorem Production Tax Refund Made
by Mobil Oil Corporation**

ISSUE DATE: August 14, 2000

DOCKET NO. G-999/AA-98-332

ORDER EXTENDING VARIANCES

PROCEDURAL HISTORY

On September 10, 1997, the Federal Energy Regulatory Commission (FERC) issued an order that required producers to refund to certain interstate pipelines all Kansas ad valorem tax amounts included in the wholesale price of natural gas sold in interstate commerce from October 1983 to June 1988, if inclusion resulted in prices that exceeded the applicable maximum lawful price for such gas under the Natural Gas Policy Act of 1978 (NGPA). FERC also required producers to refund interest on these excess revenues.

On November 10, 1997 Northern Natural Gas Company (Northern) submitted its Statement of Refunds Due to FERC. Almost all of the refund amounts stated by Northern have been disputed by the producers and other parties.

On December 30, 1997, Mobil refunded, under protest, approximately \$30 million to Northern Natural Gas Company, the interstate pipeline. Other producers placed funds into escrow instead of making refunds to the pipelines, as permitted by FERC in subsequent orders, pending final resolution of this issue.

On January 29, 1998, Northern refunded to its customers by check the money it received from Mobil. This refund included approximately \$12.1 million for Minnesota jurisdictional gas utilities. Additional smaller amounts were received from Mobil and other producers after January 29, 1998.

On March 13, 1998, the Minnesota Department of Public Service (now the Department of Commerce) requested a variance to the supplier refund rules, Minn. Rules, part 7825.2700, subpart 8, for all Minnesota gas utilities.¹ The requested variance would allow the utilities to defer refunding the Kansas ad valorem production tax refund received in January 1998.

On June 2, 1998, the Commission issued its ORDER GRANTING VARIANCES, REQUIRING INTERIM REPORT AND REFUND PLANS in this docket. The Order granted a variance for nine months from the date of the meeting (i.e. until January 23, 1999) and required a report due October 23, 1998.

On January 26, 1999, the Commission issued its ORDER EXTENDING VARIANCE. The Order extended for 18 months, until July 23, 2000, the variance granted in the Commission's June 2, 1998 Order. The Minnesota gas utilities (the Industry) were required to file a status report on the Congressional and legal proceedings and the investment status of the funds (principal, interest, specific investments) and a refund plan three months prior to the expiration of the variance extension.

On April 24, 2000, Industry submitted its compliance filing recommending an extension of the variance granted by the Commission in its January 26, 1999 Order, until December 1, 2001 with a status report due October 1, 2001. In its compliance filing, Industry proposed a refund plan that included all current sales and transportation customers. Industry submitted an Amended Attachment A to its compliance filing on April 25, 2000.

On May 22, 2000, the Department of Commerce (DOC) submitted comments recommending the variance be extended until December 1, 2001 with a status report due September 1, 2001.

On May 22, 2000, the Office of Attorney General-Residential Utilities Division (OAG) submitted comments recommending that the Commission deny an extension of the variance and require a refund. In its comments, OAG opposed Industry's plan to include transportation customers in the refund.

On June 5, 2000, the Large Power Interveners (LPI)² submitted reply comments supporting an extension of the variance and Industry's proposed refund plan.

On June 5, 2000, the Industry submitted reply comments.

¹ The Minnesota gas utilities (local distribution companies or LDCs) are: Great Plains Natural Gas Company; Alliant Utilities (Interstate Power Company); Northern States Power Company-Gas Utility including Western Gas Utilities; Peoples Natural Gas Company and Northern Minnesota Utilities, Divisions of UtiliCorp United, Inc.; and Reliant Energy Minnegasco. These companies are also referred to in this Order as the "gas utilities" or "the Companies" or "the Industry."

² Eveleth Mines LLC (dba EVTAC Mining), Hibbing Taconite Joint Venture, Ispat Inland, Inc., LTV Steel Mining Company, National Steel Pellet Company, Northshore Mining Company, and USX Corporation.

On June 7, 2000, the Industry submitted its response to information request-litigation history.

On July 13, 2000, the Commission met to consider this matter.

FINDINGS AND CONCLUSIONS

I. Introduction

As of March 31, 2000, Minnesota LDC's were holding, in separate external interest-bearing accounts, approximately \$16, 421,000 in principal and interest related to the refund of Kansas ad valorem taxes. The interest-bearing accounts are earning less than the prime rate.

In this Order, the Commission will consider whether to grant the Industry's request to continue the variances granted in the Commission's June 2, 1998 Order in this matter, and extended in the Commission's January 26, 1999 Order, to allow the utilities to defer refunding the Kansas ad valorem production tax refunds received since January 1998 for an additional 18 months.

II. Status of Litigation, Settlement Discussions and Other Issues

A. Litigation

Many issues involving the ad valorem refunds continue to be litigated.

The D.C. Circuit Court in Anadarko Petroleum Corporation v. FERC³ affirmed: 1) that the Kansas tax should not have been recovered in prices in excess of the NGPA maximum lawful price; 2) that producers had notice this practice could be improper after October 4, 1983; 3) that collection by producers of tax reimbursements from the pipeline customers after that date, whether by lump-sum transactions or other means, was unlawful; and 4) producers must refund the amounts collected with interest where the tax reimbursements caused the sale to exceed the NGPA maximum lawful price.

On June 5, 2000, the U.S. Supreme Court denied Anadarko's petition for a writ of certiorari, thereby sustaining the D.C. Circuit's decision.

³ 196 F.3d 1264 (D.C.Cir.1999), 200 F.3d 867 (D.C. Cir. 2000).

There is before the Kansas District Court⁴ a challenge to FERC's authority to order ad valorem refunds in light of a 1998 Kansas statute. The Kansas statute⁵, among other things, declared refunds claimed to be owed by royalty owners uncollectible. FERC, however, held that the Kansas statute did not relieve the producer of its refund obligation attributable to the amount paid to the royalty interest owner.⁶

Pending in Federal District Court in Texas is an ongoing dispute between Anadarko Petroleum Corporation and PanEnergy Pipeline regarding the parties' ad valorem tax refund obligations.

In addition there are several proceedings pending before FERC involving the ad valorem refunds.

B. Settlement Offers

Several proposed unilateral offers of settlement (i.e., an offer to settle that no party has accepted) have been filed with FERC.

- On March 8, 2000 Colorado Interstate Gas (CIG) and Public Service Company of Colorado (PSCo) filed a unilateral settlement offer with FERC seeking to resolve all claims of CIG with non-contesting producers.⁷ The offer proposed to forgive 12.5% of each consenting working interest owner's refund liability for each working interest owner, and would implement an additional reduction of \$10,000, unless a lesser amount would extinguish liability.
- On March 21, 2000 the National Gas Committee of the Kansas Independent Oil and Gas Association (KIOGA) countered the CIG proposal. KIOGA proposed waiving 25% of each claim across the board for principal and interest and giving each individual working interest an additional credit of \$75,000. All claims pertaining to royalty interests would be released.

⁴ Plains Petroleum Co. and Plains Petroleum Operating Company v. 1st National Bank of Lamar, et al., 99 CV 13 (District Court, Stevens County, Kansas).

⁵ K.S.A. 1999 Supp. 55-1624.

⁶ The royalty owner is usually the landowner and typically receives 12.5% of the proceeds from the well.

⁷ Colorado Interstate Gas Company, Docket No. RP98-54-029.

- Two other offers of settlement have been filed with FERC.⁸ In both of these offers the pipeline companies have offered to forgive up to \$50,000 of refunds from each producer.

The Kansas Corporation Commission and FERC's Office of Dispute Resolution recently sponsored two industry-wide settlement conferences held on March 13 and 28, 2000. Settlement conferences specific to Northern were held on May 9 and June 20, 2000, on the issue of refunds of the ad valorem tax. A further meeting was scheduled for July 18, 2000.

C. Other Issues

Verification of the actual total amount of refund liability and each producer's (or first seller's) responsibility continues to be extremely difficult. The pipeline's records of its transactions from 1983 through 1988 are not complete or in good condition, employees have retired or died, potentially liable parties have not been entirely cooperative, and some of the potentially liable parties are deceased, out-of-business or bankrupt.

III. Variance

A. Background

In its June 2, 1998 Order, the Commission granted the Industry a variance until January 23, 1999. This variance was extended in the Commission's January 26, 1999 Order. At the Department's request, the Commission varied the requirement of Minn. Rules, Part 7825.2700, Subpart 8 that supplier refunds exceeding \$5.00 per customer be made within 90 days of the date the refund is received from a supplier or transporter and the requirement that unrefunded balances accrue interest at the prime rate. In granting this variance, the Commission relieved the gas utilities of their obligation under the cited rule to make supplier refunds related to the Kansas ad valorem tax refund within the 90 day period and their obligation to accrue interest at the prime rate on the unrefunded balances.

The Commission granted the variance, and the extension of the variance, because, due to ongoing disputes between Northern and its suppliers over the total dollar amount and between Northern and its customers over the allocation of the refund, the final amount of the refund could not be reasonably determined. As a consequence, if the refund had been made as required by the rule, there was a real possibility that the gas utilities would have to either surcharge their customers for any amount they were overpaid or absorb the difference. To avoid the potential for customer confusion, then, as well as the real possibility of an unnecessary expenditure of time and money due to a surcharge, the Commission granted the variance.

⁸ Panhandle Eastern Pipeline Company, Docket No. RP98-40-024 and Williams Gas Pipelines Central, Inc., Docket No. RP98-52-036.

Now, as the variance as extended in the January 26, 1999 Order expires, the Commission must consider whether to extend the variance or let it lapse and order an immediate refund.

B. Positions of the Parties

1. The Industry

The Commission-rate regulated gas utilities (the LDC's or the Industry) recommended that the variances be extended until December 1, 2001 with a status report due on October 1, 2001. The Industry argued that the following issues need to be resolved before the Industry is ordered to issue refunds to ratepayers:

- pending appeals that challenge past adjudicated decisions,
- actual determinations of amounts owed and the responsible parties,
- the authority of Kansas state law to determine that the ad valorem tax refund is "uncollectible" against certain entities.

The Industry argued that there has been no further resolution of the issues surrounding the ad valorem tax refund since the Commission's last order extending the variance.

The Industry indicated that even with the U.S. Supreme Court's action in Anadarko v. FERC there are numerous issues still unresolved. The Industry indicated that there are multiple pending legal actions and settlement discussions that will affect the amount of ad valorem tax refund to Minnesota ratepayers. The Industry agreed with the DOC that waiting until these issues are resolved will avoid the possibility of a surcharge being necessary at a later date.

2. The Department of Commerce

The DOC recommended that the variances be extended until December 1, 2001, but suggested that the Industry status report should be filed on September 1, 2001. The DOC indicated that the situation appears no closer to resolution now than it did in January 1999 when the Commission last reviewed this matter.

The DOC indicated that the Mobil refund amounts are being securely held for customers, with interest accruing upon them, and at no benefit to the utilities. The most reasonable approach, according to the DOC, is for the Commission to defer requiring a refund until it is reasonably sure that a later surcharge will not be necessary.

3. The Office of Attorney General - Residential Utilities Division

The OAG opposed the Industry's request for an extension of the variances until December 1, 2001. The OAG recommended that refunds should be made immediately once the U.S. Supreme Court denied the petition for a writ of certiorari in Anadarko v. FERC.⁹ The OAG argued that a final ruling from the U.S. Supreme Court upholding FERC's ruling on the Kansas ad valorem tax will provide a sufficient degree of certainty so that ratepayers should receive refunds at that time. Further, Minnesota ratepayers should not have to wait until the gas producers have fully litigated every possible issue to receive the refunds.

4. Large Power Interveners

The Large Power Interveners (LPI) supported the Industry's request to extend the variance.

IV. Commission Action

The Commission is not persuaded that it should abandon what it believes is a prudent approach to this matter, to defer the refund until it is reasonably clear that a surcharge is not a substantial concern. Even though the U.S. Supreme Court has denied a petition for a writ of certiorari in Anadarko, the Commission recognizes that the numerous pending appeals and ongoing settlement negotiations continue to make the issue of the amount and collection of these refunds uncertain. Further, the costs of refunding and surcharging, if this becomes necessary, would be substantial. The Commission notes that the potential refund amounts are securely held for customers, with interest at market rates accruing on them, at no benefit to the utilities.

In these circumstances, the Commission continues to believe that the most responsible approach is to defer requiring a refund until the Commission can be reasonably sure that a later surcharge will not be necessary. The prerequisites for a variance, as set forth in Minn. Rules, Part 7829.3200, which were found to have been met in the June 2, 1998 Order (granting the variances) and the January 26, 1999 Order (continuing the variances) continue to be met for the reasons set forth in that Order.¹⁰ The Commission, therefore, will extend the variances until December 1, 2001 and require the Industry to file a status report on legislative activity, legal proceedings and the investment status of the funds by September 1, 2001.

The Commission believes that in light of the extension granted in this Order it is premature

⁹ The comments of the parties were all made prior to the U.S. Supreme Court's June 5, 2000 denial of the petition for a writ of certiorari in Anadarko v. FERC, and included recommended future action depending on the Supreme Court's later decision.

¹⁰ See June 2, 1998 ORDER GRANTING VARIANCES, REQUIRING INTERIM REPORT AND REFUND PLANS

to adopt a refund plan at this time.

ORDER

1. The variances granted in the Commission's June 2, 1998 Order in this matter, and extended in the Commission's January 26, 1999 Order, which were set to expire on July 23, 2000, are extended until December 1, 2001.
2. The Minnesota gas utility companies referred to in this Order as the Industry shall file another status report on legislative activity, legal proceedings and the investment status of funds (i.e. principal, interest, specific investments) by September 1, 2001.
3. The Executive Secretary shall have the authority to set time periods and filing procedures for comments and replies and to vary the time periods, if necessary.
4. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Burl W. Haar
Executive Secretary

(S E A L)

This document can be made available in alternative formats (i.e., large print or audio tape) by calling (651) 297-4596 (voice), (651) 297-1200 (TTY), or 1-800-627-3529 (TTY relay

service).